

WATER/IRJ/ABJ:jrb

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

WATER DIVISION
Advisory Branch

RESOLUTION NO. W-4320
January 23, 2002

R E S O L U T I O N

(RES. W-4320), SOUTHERN CALIFORNIA WATER COMPANY (SCWC), METROPOLITAN DISTRICT. ORDER ADDRESSING THE REQUEST TO INCREASE RATES BY USING A PRICE INDEX AND TO FINANCE ITS INFRASTRUCTURE REPLACEMENT PROGRAM.

SUMMARY

By Advice Letter (AL) 1105-W received November 13, 2001, SCWC requests the authority to increase rates in its Metropolitan district by \$3,127,962 or 4.2% to offset an increase in rate base due to its Infrastructure Replacement Program (IRP) and offset increased costs by using a price index. This resolution explains and approves those requests.

BACKGROUND

In its last general rate case for its Metropolitan district (D.98-12-070 in A.98-03-029 et. al.) SCWC and staff presented a Stipulation (Appendix D to the Decision) that was adopted by the Commission in ordering paragraph 2. Three sections of that stipulation relate to this filing.

“17.04 The Costs of Replacing Infrastructure - - The Parties agree to a modified Infrastructure Replacement Program. The Parties agree that SCWC should have the option of extending the Metropolitan’s rates through the year 2003. The costs of replacing infrastructure could be recovered through Advice Letter in 2001, 2002, and 2003. An increase in authorized expenses during the extended period would be allowed based on the most current Price Index (as defined in 17.06). The Parties agree to a band on earnings of 200 basis points either way. Advice Letters will be subject to the revised proforma test on earnings which will be determined at a later date.

“17.05 Established Factors - - Established Factors will be comprised of the following factors, which are published on a monthly basis: 1) the Compensation Per Hour Index, and , 2) the NonLabor Index (both published in a memo from the ORA Monopoly Regulation Branch to the Water Division of the Commission.

“17.06 Price Index – Infrastructure Replacement - - The Price Index will be comprised of the following three factors, which are published on a monthly basis: 1) the Compensation Per Hour Index, 2) the Non-Labor Index both published in a memo from the ORA Monopoly Regulation Branch to the Water Division of the Commission, 3) the Construction Cost Index as printed in Engineering & News Reports. Each factor is weighted one-third. The Price Index will determine the maximum change from the prior years rates.”

In its filing SCWC calculates the price index for 2002 as 2.2% using the ORA Compensation Per Hour and Non-Labor Indices as of August, 2001 and the Construction Cost Index as of October, 2001. It applies this inflator to operations and maintenance expenses (excluding offsettable expenses) but only for those expenses that might be expected to increase due to cost pressures. For example, SCWC does not increase postage. The resulting index-driven increase in expenses after being grossed-up for taxes is \$961,000.

It next lists the projects that it plans to complete in calendar year 2002. The projects include two new wells, one called Central and one called Southwest, for \$1,800,000 each and shows a detailed list of main replacement projects, with the sections and streets identified and the length of the replacement specified. The total expected costs for main replacements is \$8,214,400. The total IRC budget, with an additional 10% for contingencies is \$12,995,840. SCWC determined rate base impact of these additions by calculating a dollar return on rate base using the latest rate of return authorized for SCWC in D.00-12-063. After grossing-up for tax impacts, the annual revenue requirement for the IRP is \$2,166,962.

The request totals \$3,127,962.

DISCUSSION

The language in the stipulation is vague at best as to *how* the provisions of these three paragraphs are to be calculated, but the methods that SCWC has chosen to use are based upon standard ratemaking methods. This is important because there was no information contained in the decision or stipulation that shows how these adjustments were to apply. Staff has no problems with the methods SCWC has chosen to use and believe they adequately follow the intent of the stipulation.

Staff's real concern is more of a policy issue. Standard monopoly ratemaking is based on the precept that new plant investments are not allowed into rates until the facilities are "used and useful." In this filing, as addressed in the stipulation, SCWC proposes to place in rates facilities it has yet to build. Although there is no reason to believe SCWC will not complete all the projects it proposed in its IRP for 2002, it is possible that some will not be built, and that the final costs of construction will be different (both higher or lower) than the IRP anticipates.

On the other hand, the Commission itself, because it uses a future test year, allows facilities that have yet to be built in the first and second test years to be reflected in rates for those years. Arguably, this concept could also be applied to the years after the test years, as in this case, rather than requiring the utility to file a rate base offset.

Staff has some concerns though. If, through no fault of SCWC, problems do occur that result in an actual rate base increase of less than that proposed in this advice letter, customers will be paying for facilities that don't yet exist. Therefore staff recommends that SCWC should book the revenues actually received from the \$2,166,962 increase in revenue requirement that this resolution allows in calendar year 2002 to a memorandum account. In early 2003, SCWC will file an advice letter to allow it to book these revenues by calculating the allowable amounts based upon actual monthly values of IRP-based incurred investment. If the utility deserves the entire amount or more, the memorandum account will be closed and the revenues can be booked. If the actual investments do not support the entire revenue requirement, the utility would file, in the same advice letter, a plan to refund the excess. Staff has contacted SCWC and the utility agrees with this limitation.

NOTICE AND PROTESTS

The original advice letter was sent to nearby municipalities and water utilities. Notice of the increase was published as a legal notice in newspapers and sent to customers on November 16, 2001. No protests have been received.

FINDINGS AND CONCLUSIONS

1. D.98-12-070 approved a stipulation in the general rate increase request for Southern California Water Company, Metropolitan District.
2. The stipulation allowed for rate changes in the year after the attrition year (year four) and the year after that (year five) based on a price index applied to certain expenses and taxes.
3. The stipulation allowed for rate changes in the year after the attrition year (year four) and the year after that (year five) to track anticipated additions to rate base in those years.
4. The stipulation did not specify the procedures for calculating the increases, but the filing follows normal ratemaking practices.
5. It is possible that the additions to rate base in year four and year five will deviate from those projected.
6. It is reasonable to require SCWC to track actual revenues in a memorandum account. Prior to April 1, 2003, SCWC shall file an advice letter to "true-up" the account balance with what would have been received if SCWC had added its IRP facilities installed in each month of the year to rate base. The advice letter shall request to refund any collections in excess.

THEREFORE IT IS ORDERED THAT:

1. Southern California Water Company is authorized to make effective revised Schedule No. ME-1, General Metered Service, attached to Advice Letter No. 1105-W, and to cancel its presently effective rate schedule. The effective date of the revised rate schedule shall be five days after the effective date of this resolution.

2. Southern California Water Company, Metropolitan District, shall record the revenues actually received from the \$2,166,962 increase in revenue requirement that this resolution allows in calendar year 2002 (and thereafter) in a memorandum account until said memorandum account is closed as provided in Ordering Paragraph 3.
3. Prior to April 1, 2003, Southern California Water Company, Metropolitan District, shall file an advice letter to "true up" the memorandum account balance with the actual revenue requirement (revenue that would have been received if Southern California Water Company, Metropolitan District had added its Infrastructure Replacement Program facilities installed in each month of the year to rate base). If the memorandum account balance is equal to or less than the actual revenue requirement, the memorandum account balance shall be recorded as revenue and the memorandum account closed. If the memorandum account balance is greater than the actual revenue requirement, the utility shall file, in the same advice letter, a plan to refund the excess and upon implementation of said refund, the memorandum account shall be closed.
4. This resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on January 23, 2002; the following Commissioners voting favorably thereon:

WESLEY M. FRANKLIN
Executive Director